

REPORT OF THE AUDITOR-GENERAL TO THE LIMPOPO PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE LEPELLE- NKUMPI LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the financial statements of the Lepelle-Nkumpi Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2013, the statements of financial performance, changes in net assets and cash flows for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), and the Division of Revenue Act of South Africa, 2012 (Act No.5 of 2012) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer opinion

Property, plant and equipment

4. I identified a significant number of assets belonging to the municipality that were not accounted for in the accounting records and financial statements. The total value of the unrecorded assets could not be determined. Consequently, it was impracticable to determine the extent of the understatement of the property, plant and equipment balance of R465 607 702 stated in note 7 to the financial statements.
5. I identified completed projects amounting to R 48 261 923 in the accounting records that are still classified as work in progress. I was unable to confirm whether all completed projects were correctly classified and treated in accordance with accounting standards. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed as work in progress (R61 033 483), depreciation (R26 078 999) and accumulated depreciation (R124 650 143) as stated in note 7 to the financial statements.
6. The municipality did not classify completed projects as property, plant and equipment where the projects are substantially ready for use in accordance with the SA Standards of GRAP 17, *Property, plant and equipment*. I identified completed projects amounting to R10 769 120 for which the total costs were not fully recorded in the accounting records and financial statements. I was unable to determine whether any further adjustments were necessary to the amount disclosed as property, plant and equipment as stated in note 7 at R465 607 792 to the financial statements.
7. The underlying accounting records of the municipality did not include sufficient information to enable me to obtain appropriate audit evidence to verify existence of work in progress amounting to R11 418 015. The municipality's records did not permit the application of alternative audit procedures regarding the projects. Consequently, I was unable to determine whether any adjustments were necessary to the amount disclosed as work in progress as stated at R61 033 483 in note 7 to the financial statements.

8. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect to property, plant and equipment amounting to R384 945 050 as disclosed in note 7.2 to the financial statements. I was unable to confirm the possible misstatement on property, plant and equipment. Consequently, I was unable to determine whether any adjustments to property, plant and equipment were necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.
9. Additionally, with reference to the above paragraphs, I was unable to verify the accuracy of the depreciation disclosed in note 7 to the financial statements amounting to R26 078 999 (2012: R14 909 674) and the corresponding accumulated depreciation amounting to R124 650 153 (2012: R 146 028 524).

Revenue

10. The SA Standards of GRAP 23, *Revenue from non exchange transactions*, requires that revenue from fines should be based on actual revenue received as well as an estimate of spot fines and summonses issued based on past experience of amounts collected. The municipality did not make an estimate of spot fines and summonses issued based on past experience of amounts collected. I was unable to determine the extent of the fines estimate by alternative means. Consequently, I was unable to determine whether any adjustment to fines issued of R624 895 as disclosed in the statement of financial performance were necessary.
11. Included in revenue from water and sanitation agency fees of R29 333 436 is a journal entry of R17 747 822 for which I could not obtain sufficient appropriate audit evidence. I was unable to confirm this amount by alternative means. Consequently, I was unable to determine whether any further adjustments to revenue from water and sanitation agency fees of R29 333 436 as stated in note 19 to the financial statement were necessary.
12. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect of revenue from property rates amounting to R48 630 227 as disclosed in note 14 to the financial statements. Consequently, I was unable to determine whether any adjustments to revenue from property rates were necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Trade and other receivables from exchange transactions

13. Included in trade and other receivables balance of R36 629 637 is a journal entry of R17 969 044 for which we could not obtain sufficient appropriate audit evidence. I was unable to confirm this amount by alternative means. Consequently, I was unable to determine whether any further adjustments to trade and other receivables of R36 629 637 as stated in note 2 to the financial statements were necessary.
14. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect of trade and other receivables and impairments from exchange transactions amounting to R98 279 525 and R56 779 807 respectively, as disclosed in note 2 to the financial statements. I was unable to confirm the possible misstatement on trade and other receivables from exchange transactions. Consequently, I was unable to determine whether any adjustments to trade and other receivables from exchange transactions were necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Other receivables from non-exchange transactions

15. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect of other receivables from non exchange transactions amounting to R53 275 197 as disclosed in note 3 to the financial statements. Consequently, I was unable to determine whether any adjustments to other receivables from non-exchange transactions were necessary. My audit opinion on the

financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Trade and other payables from exchange transactions

16. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect of retentions and deferred income amounting to R12 223 952 and R17 747 822 respectively as disclosed in note 8 to the financial statements. Consequently, I was unable to determine whether any adjustments to retentions and deferred income were necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Valued added tax (VAT) receivable

17. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect of VAT receivable amounting to R4 986 922 as disclosed in note 10 to the financial statements. I was unable to confirm the possible misstatement on VAT receivable. Consequently, I was unable to determine whether any adjustments to VAT receivable were necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Aggregation of immaterial uncorrected misstatements

18. The following misstatements, individually immaterial but in aggregate material, were not corrected in the 2012 comparative figures to the financial statements;

- Other creditors reflected as R3 416 261 is understated by R3 416 261
- Staff leave accrual reflected as R 3 023 805 is understated by R3 023 805

As a result, I was unable to determine whether any adjustments to these elements were necessary.

Cash flow statement

19. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect of increase in net cash and cash equivalents amounting of R 16 417 232 as disclosed in the cash flow statement. Consequently, I was unable to determine whether any adjustments to increase in net cash and cash equivalents were necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Contingent liabilities

20. Included in contingent liabilities of R365 089 458 as disclosed in note 40 to the financial statements are transactions amounting to R362 244 458 that do not meet the definition of a contingent liability as defined in terms of SA standards of GRAP 19, *Provisions, contingent liabilities and contingent assets*. Consequently, contingent liabilities in the financial statements are overstated by R362 244 458
21. The municipality has not disclosed a contingent liability in respect of the uncertainties arising from the dispute declared by the unions and the pending litigation regarding the wage curve agreement. I was unable to confirm the contingent liabilities by alternative means. Consequently, I am unable to determine whether any adjustments to contingent liabilities stated at R365 089 458 in note 40 to the financial statements was necessary.
22. During 2012, I was unable to obtain sufficient appropriate audit evidence in respect of contingent liabilities amounting to R3 118 467 as disclosed in note 40 to the financial statements. Consequently, I was unable to determine whether any adjustments to contingent liabilities were

necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Unauthorised expenditure

23. During 2012 unauthorised expenditure amounting to R13 916 876 was not disclosed in the financial statements. Consequently, unauthorised expenditure as disclosed in the financial statements was understated by R13 916 876. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the effect of this matter on the comparability of the current period's figures.

Commitments

24. During 2012, I was unable to obtain sufficient appropriate audit evidence with respect of commitments amounting to R4 986 922 as disclosed in note 37 to the financial statements. I was unable to confirm the possible misstatement on commitments. Consequently, I was unable to determine whether any adjustments to commitments were necessary. My audit opinion on the financial statement for the period ended 2012 was modified accordingly. My opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Disclaimer of opinion

25. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

Emphasis of matters

26. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

27. As disclosed in note 34 to the financial statements, the corresponding figures for 30 June 2012 have been restated as a result of an error discovered during 2013 in the financial statements of the municipality at, and for the year ended, 30 June 2012.

Impairments

28. The municipality had trade and other receivables from exchange transactions totalling R116 092 071 as at 30 June 2013 of which R79 462 432 was provided for as debts impairment provision as disclosed in note 2 to the financial statements.

Additional matters

29. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited supplementary schedules

30. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

Withdrawal from the audit engagement

31. Due to the limitation imposed on the scope of the audit by management, I have disclaimed my opinion on the financial statements. But for the legislated requirement to perform the audit of the municipality, I would have withdrawn from the engagement in terms of the ISAs.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

32. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

33. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
34. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury *Framework for managing programme performance information (FFPPI)*.
35. The reliability of the information in respect of the selected development objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

The material findings are as follows:

Usefulness of information

Presentation

Measures taken to improve performance not disclosed

36. Section 46 of the Municipal Systems Act 2000, (Act No.32 of 2000) (MSA) requires disclosure in the annual performance report of measures taken to improve performance where planned targets were not achieved. Measures to improve performance for a total of 100% of the planned targets not achieved were not reflected in the annual performance report. This was due to the lack of review of the presentation of the annual performance report by management.

Consistency

Reported objectives not consistent with the planned objectives

37. The MSA, section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 56% of the reported objectives are not consistent with the objectives as per the approved integrated development plan (IDP). This is due to the lack of review of the reported performance information by management.

Reported indicators not consistent with planned indicators

38. The MSA, section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 44% of the reported indicators are not consistent with the indicators as per the approved service delivery agreement. This was due to a lack of review of and monitoring over the completeness of reporting documents by management.

Reported targets not consistent with planned targets

39. The MSA, section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 40% of the reported targets are not consistent with the targets as per the approved IDPs. This was due to a lack of review of and monitoring over the accuracy and completeness of reporting documents by management.

Changes to development objectives, indicators and targets not approved

40. A total of 100% of development objectives, indicators and targets reported in the annual performance report were changed in-year without following the process as prescribed in section 34 of the Municipal Systems Act and without adoption by the council of the municipality. This was due to the fact that the changes to the IDP were implemented without the council's approval.

Measurability

Performance targets not specific

41. The National Treasury *FMPPi* requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 29% of the targets were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.

Performance targets not measurable

42. The National Treasury *FMPPi* requires that performance targets be measurable. The required performance could not be measured for a total of 29% of the targets. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.

Performance indicators not well defined

43. The National Treasury *FMPPi* requires that indicators should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 92% of the indicators were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.

Performance Indicators not verifiable

44. The National Treasury *FMPPi* requires that it must be possible to validate the processes and systems that produce the indicator. A total of 20% of the indicators were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.

Reliability of information

Reported performance not reliable

45. The National Treasury (*FMPPi*) requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets.

Significantly important targets with respect to technical and community service are materially misstated. This was due to the lack of standard operating procedures for the accurate recording of actual achievements.

Additional matter

46. I draw attention to the following matter below. This matter does not have an impact on the predetermined objectives audit findings reported above.

Achievement of planned targets

47. Of the total number of 183 targets planned for the year, 105 of targets were not achieved during the year under review. This represents 57% of total planned targets that were not achieved during the year under review. This was mainly due to the fact that Service Delivery and Budget

Implementation Plan indicators and targets were not consistent with the annual report indicators and measures.

Compliance with laws and regulations

48. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Strategic planning and performance management

49. The annual performance report for the year under review does not include measures taken to improve performance, as required by section 46 (1)(c) of the MSA..

Annual financial statements, performance and annual reports

50. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors were not adequately corrected, which resulted in the financial statements receiving a disclaimer audit opinion.
51. The 2011-12 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.

Procurement and contract management

52. Goods and services with a transaction value of below R 200 000 were procured without obtaining the required price quotations as required by Supply Chain management (SCM) regulation 17 (a) and (c).
53. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy in contravention of SCM regulation 16(b) and 17(b)
54. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2).
55. Contracts were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding, in contravention of SCM Regulations 21(b) and 28(1)(a) and the Preferential Procurement Regulations.

Revenue management

56. An effective system of internal control for debtors was not in place, as a required by section 64(2)(f) of the MFMA.

Expenditure management

57. An effective system of expenditure control including procedures for the approval was not in place, as required by section 65(2)(a) of the MFMA..
58. The accounting officer did not take effective steps to prevent irregular expenditure and fruitless and wasteful expenditure, as required by section 95(d) of the MFMA.

Asset management

59. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.
60. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 96(2)(a) of the MFMA.

Human resource management

- 61. An acting chief financial officer (CFO) was appointed for a period of more than six months, in contravention of section 56(1)(c) of the MSA.
- 62. Senior managers directly accountable to the municipal manager did not sign performance agreements, as required by section 57(2)(a) MSA.

INTERNAL CONTROL

- 63. I considered internal control relevant to my audit of the financial statements, performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion, the findings on the performance report and the findings on compliance with laws and regulations included in this report.

Leadership

- 64. Management did not always exercise an appropriate level of oversight regarding financial and performance reporting, compliance and related internal controls.
- 65. Action plans were developed in the prior year, however, the implementation of the recommendations from internal and external audit were not addressed, hence the recurrence of findings identified in the prior year with regard to property, plant and equipment and unresolved prior year issues.

Financial and performance management

- 66. Controls over daily and monthly processing and reconciling of transactions were not implemented by the accounting officer
- 67. Compliance with laws and regulations was not reviewed and monitored by the accounting officer.

Governance

- 68. Management ineffectiveness in implementing recommendations from internal and external audit did not enable the audit committee to promote accountability and service delivery through evaluating and monitoring responses to risks and providing oversight over the effectiveness of the internal control environment, including financial and performance reporting and compliance with laws and regulations.

Other reports

Investigations

- 69. An investigation was conducted in 2013 by the municipality's internal audit unit regarding allegations of misuse of the municipality's petrol cards by certain officials. The matter was referred to South African Police Services (SAPS). The investigation was still on-going at the date of my report.

Auditor-General

Polokwane

12 February 2014



AUDITOR-GENERAL
SOUTH AFRICA

And try to build public confidence